

**Before the  
Federal Communications Commission  
Washington, D.C. 20554**

|   |   |                     |
|---|---|---------------------|
| In the Matter of                          | ) |                     |
|   | ) |                     |
| Petition for Declaratory Ruling and Other | ) | CC Docket No. 96-45 |
| Relief of ACS of Fairbanks, Inc.          | ) |                     |
|   | ) |                     |

**OPPOSITION OF GENERAL COMMUNICATION, INC. TO PETITION FOR  
DECLARATORY RULING AND OTHER RELIEF OF ACS OF FAIRBANKS, INC.**

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## SUMMARY

ACS of Fairbanks, Inc. (“ACS-F”) is seeking a rule change in the guise of a declaratory ruling. ACS-F petitions the Commission to declare that “no competitive eligible telecommunications carrier (“CETC”) shall receive interstate high-cost loop support if its loop costs lie below the FCC high-cost standard, set at approximately \$23.00 per line per month” and to order the Universal Service Administrative Company to “suspend any payment of interstate high-cost support to any CETC that does not satisfy the test for high-cost loops established by the Commission.” But there is no ambiguity for the Commission to address: Section 54.307(a)(2) of the Commission’s rules specifically directs that a CETC using an unbundled ILEC loop to provide supported services shall receive “the lesser of the unbundled network element price for the loop or the incumbent LEC’s per-line payment from high-cost loop support and LTS.” Indeed, throughout the petition, ACS-F repeatedly acknowledges that current disbursement of USF support to its competitor, General Communication, Inc. (“GCI”), is fully authorized by the Commission’s rules.

Faced with the clarity of the Commission’s rules, ACS-F attempts to bootstrap an unbundled network element (“UNE”) price limitation onto section 254(e)’s requirement that “[a] carrier that receives such [universal service] support shall use that support only for the provision, maintenance, and upgrading of facilities and service for which the support is intended.” ACS-F argues that the “service for which support is intended” is service by carriers with loops of greater than \$23.00 per month in embedded cost. This argument, however, rewrites the definition of a supported service that was proposed by the Federal-State Joint Board and adopted by the Commission. Supported services are defined in the Commission’s rules in terms of type and quality of service – single-party, voice-grade access to the public switched network, with certain

required features. There is no cost or UNE price component to the definition of a supported service. This is but another attempt by ACS-F to have the Commission rewrite its rules without rulemaking – something the Commission cannot do.

Even if ACS-F were not asking the Commission to rewrite the rules via declaratory ruling, the Commission should still reject ACS-F's requested relief as anti-competitive and anti-consumer. ACS-F ignores entirely that the Commission expressly – and with good reason – rejected the idea that CETCs should receive universal service support based on CLEC costs, rather than based on the ILEC's support. The Commission's existing approach is entirely consistent with the goals and purposes of the Act. It is competitively neutral because it preserves parity in the forward-looking cost of the UNE loop to all competitors, rather than subsidizing just one, and thus does not distort the competitive market or the price signals to competitors. In fact, section 54.307 preserves exactly the same price signals that would exist in the market if there were no USF support for either carrier.

Setting USF loop support for CLECs based on the CLECs' own costs, on the other hand, would be anti-competitive and unworkable, and would coddle inefficiency and poor decision-making. In order to implement such a system, moreover, the Commission would have to institute extensive cost regulation of each CLEC. Contrary to the blithe assertions of ACS-F, a CETC's costs do not consist solely of the price paid for ILEC UNE loops, even for those CLECs that rely extensively on UNE loops. For example, the ILEC UNE loop comprises only a portion of GCI's loop facilities and costs. GCI also provides a portion of its loop – the portion from GCI's switch to its collocation equipment at ACS-F's switch or remote<sup>1</sup> – using its own facilities, including digital loop carriers, fiber terminals, DSX cross connects, cable and ducts.

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<sup>1</sup> See Declaration of Frederick W. Hitz, III ("Hitz Declaration"), attached hereto as Exhibit 1, at ¶ 6.

Furthermore, GCI provides significant service entirely with its own loops, without UNEs from ACS-F. ACS-F's simplistic fixation on UNE loop rates ignores these other costs of facilities-based competition.

Even if the Commission were to engage in the extensive regulatory oversight necessary to calculate CETCs' actual total loop costs, using CETC costs as a basis for CETC high cost loop support while subsidizing the ILEC based on its embedded costs would undermine positive competitive pressures. Such a system eliminates incentives to control costs, eliminates the ability of the invisible hand of the market to reveal inefficiencies that regulators may not have discovered, and, instead, rewards inefficiency by giving the CETC the same inappropriate incentive to inflate costs that has existed for ILECs under rate base/rate of return regulation. If a CLEC simply loses USF support when it cuts costs through efficiencies, the CLEC has no incentive to implement such cost-cutting measures.

Even worse, the system proposed by ACS-F would destroy the appropriate price signals that drive competition and force competitors to strive to deliver the highest value product at the lowest price. A system that would pay different subsidies to carriers to provide the same service to the same line would hide price signals, distorting market feedback from consumers that would otherwise select the most efficient service provider and discouraging CETCs from entering new markets, because the existing, clear price signals based on known ILEC costs would be replaced by speculative regulatory estimates of CETC costs.

ACS-F's proposed subsidy system would convert the invisible hand of the market into a very visible thumb on the scales in favor of inefficient incumbent LECs. American consumers, who ultimately pay for universal service, should not be asked to subsidize inefficient service. Instead, maintaining the same amount of portable USF support to all carriers competing to serve

the same customer retains the same cost advantage (or disadvantage) that the CLEC would have in an unsupported market. Such a result is required by the principle of competitive neutrality.

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General Communication, Inc. (“GCI”) hereby opposes the Petition for Declaratory Ruling and Other Relief (“Petition”) filed by ACS of Fairbanks, Inc. (“ACS-F”) on July 24, 2002. ACS-F petitions the Commission to issue a “declaratory ruling” requiring that interstate high-cost loop support paid to CETCs be based on the amount of the CETC’s “own per-line costs,” rather than the amount of support the ILEC would receive for service of the same line, as expressly required by the Commission’s rules. ACS-F’s petition is utterly without merit and must be denied on both procedural and policy grounds.

As an initial matter, there is no ambiguity in the rule warranting the issuance of a declaratory ruling. ACS-F’s argument is with the substance and intent of the rule itself. Indeed, ACS-F’s requested relief would entail changes to the Commission’s rules and therefore cannot be granted without a notice and comment rulemaking proceeding. Furthermore, ACS-F ignores the careful analysis the Commission undertook to ensure universal service support would be competitively neutral in effect. ACS-F’s proposed rule changes would have significant anti-competitive and anti-consumer impacts and therefore must be rejected.

As demonstrated by the plethora of pleadings that ACS-F has filed with both this Commission and the Regulatory Commission of Alaska (“RCA”), rather than evolve as an

efficient carrier in a competitive environment, ACS-F has taken an obstructionist approach. ACS-F wishes to defeat competition, and specifically its competitor GCI, through the regulatory process rather than through the market. Instead of reducing its costs or finding ways to increase consumer value, ACS-F attempts through this petition to gain an anti-competitive advantage by being the only carrier in the market to receive subsidies. In effect, ACS-F seeks to use universal service support to preserve the inefficiencies that competition is intended to eliminate. Such a result is antithetical to the Act and certainly not required by any existing rule or statutory provision.

## **I. BACKGROUND**

### **A. GCI and the Introduction of Competition in the Fairbanks Market**

GCI is a diversified telecommunications, information services, and cable television provider operating primarily in Alaska. GCI offers competitive local telephone service – along with long distance service, cable service, and high speed and dial-up Internet access – to customers in Fairbanks, competing with ACS-F, the incumbent LEC. GCI serves both the business and residential markets, meets the statutory and regulatory requirements for designation as an eligible telecommunications carrier (“ETC”), and has, in fact, been designated an ETC by the RCA.

Although GCI’s entry into Fairbanks was stalled for four years by ACS-F’s legal challenges to the RCA’s lifting of the rural exemption in this region of over 80,000 people, GCI finally was able to launch its service in the summer of 2001. And the citizens of Fairbanks have voted for competition with their pocketbooks, with GCI garnering a 17 percent market share in its first nine months by winning customers from ACS-F. Each GCI customer had a choice and



freely determined that GCI offers a better value – a higher quality service, or a lower price service, or a combination of the two.

GCI has entered Fairbanks for the long haul. Presently, GCI provides local service using all of the methods available under the Act: some customers are served entirely with GCI's own facilities; some are served using a combination of UNE loops and GCI's facilities; and some are served through total service resale, although GCI transfers as many customers as quickly as possible off of resale to UNE loops.<sup>2</sup> GCI plans eventually to migrate its customers, where possible, to service over cable telephony facilities. Cable telephony, however, is not yet a commercial, operational reality, but GCI is making substantial investments in its own loop facilities in order to free itself to the maximum extent possible from reliance on the ACS-F monopoly. It is an unfortunate reality that in order to reach its customers to provide local service *today*, GCI has no alternative to using ACS-F loops (whether through UNEs or through total service resale).

GCI's service in Fairbanks is, thus, fulfilling the primary purpose of the Act, offering competitive local exchange service to the benefit of consumers. Moreover, as anticipated by the Act, GCI is doing so with many of its own facilities, including its own switching and transport, and in some cases loop facilities, with ongoing investment in and development of its loop facilities. In that regard, GCI service in Fairbanks follows the same model as GCI's provision of comparable service in Anchorage, where GCI has gained more than a forty percent share of the

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<sup>2</sup> GCI initially launched service to many customers using total service resale, and those customers are now being converted to UNE loops. GCI now has its own switch and transport facilities in Fairbanks. For customers served with UNEs, GCI generally relies only on UNE loops from ACS-F, although GCI does serve a small number of customers via the UNE Platform in cases where GCI cannot use UNE loops or have such loops provisioned quickly enough by ACS.

local exchange service market since it began service in 1997. It should be noted that the Anchorage market receives no High Cost Loop Support.<sup>3</sup>

GCI has been successful in obtaining significant market share in local markets for a combination of reasons.<sup>4</sup> At bottom, GCI offers customers a quality product package at lower rates than the incumbent. GCI has been innovative in its customer service and service offerings, presenting customers with a package of local service plus custom calling features that is much cheaper than the price the monopolist incumbent had charged for the same set of services. GCI also combines its local service offerings with other services desired by consumers, such as Internet service, for which its extensive network also provides cost advantages. GCI has built a modern, efficient local switching and transport network, and – at least when it has not been frustrated by ACS-F’s tactics – it has been able to take advantage of economies of scale and scope in its local telephone, long distance and cable television operations in terms of installing and operating fiber optic transport facilities.

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<sup>3</sup> The Anchorage market now receives a small amount of USF support – 24 cents per residential and single-line business line – pursuant to the recently implemented Interstate Common Line Support. *See In re Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers; Federal-State Joint Board on Universal Service; Access Charge Reform for Incumbent Local Exchange Carriers Subject to Rate-of-Return Regulation; Prescribing the Authorized Rate of Return for Interstate Services of Local Exchange Carriers*, Second Report & Order & Further Notice of Proposed Rulemaking in CC Docket No. 00-256, Fifteenth Report & Order in CC Docket No. 96-45, & Report & Order in CC Docket Nos. 98-77 & 98-166, 16 FCC Rcd 19613, 19667-68 (¶ 128) (2001).

<sup>4</sup> GCI entered the market with high brand recognition and loyalty in the markets because GCI brought long distance competition, and lower rates, to Alaska. GCI also provides quality cable television service in Alaskan markets. Familiar with GCI, many customers were eager to escape the incumbent monopolist who had taken their patronage for granted for all too many years.

## **B. ACS-F's "Costs" as an ILEC**

Although ACS-F asserts that the embedded costs of a loop as carried on ACS-F's regulatory books are its "actual" costs, these costs are in no way the sort of objective, unavoidable costs that ACS-F would have the Commission believe. These embedded book "costs" are a regulatory fiction, grown out of years of state and federal ratemaking decisions and ILEC investments in a rate base rate-of-return environment that provided little incentive for cost discipline. These costs do not represent the inflated price that ACS-F chose to pay for these assets when ACS-F purchased the Fairbanks system in 1999 – after the passage of the 1996 Act, after Alaska regulators set interconnection prices in Anchorage, and after GCI requested interconnection in Fairbanks and petitioned Alaska regulators to lift the section 251(f) rural exemption in Fairbanks. ACS-F knowingly paid more than book value for the Fairbanks assets, and it did so knowing that it might be required to lease the plant to competitors at a price below its embedded costs.<sup>5</sup> Indeed, even ACS-F's purchase price in 1999 is not a true measure of ACS-F's "costs," as ACS-F's recent write-downs of goodwill in connection with those acquisitions have shown.<sup>6</sup>

The truest measure of ACS-F's "actual" costs – whether for provision to itself or to GCI – is therefore the forward-looking, cost-based rate as determined by the RCA in its Fairbanks

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<sup>5</sup> See Affidavit of Frederick W. Hitz, III, attached as Exhibit A to Opposition of General Communication, Inc. to ACS of Anchorage, Inc. & ACS of Fairbanks, Inc. Emergency Petition for Declaratory Ruling & Other Relief Pursuant to Sections 201(b) & 252 (e)(5) of the Communications Act, WC Docket No. 02-201 (filed Aug. 20, 2002), at ¶¶ 5-10 & Exhibit 1: Comparison of ATU UNE Loop Rates to Nationwide Rates.

<sup>6</sup> ACS' recent write-downs of goodwill totaled more than \$105 million across all ACS businesses, and more than \$97 million for ACS' local telephone businesses alone. See Alaska Communications Systems Group, Inc., Form 10-Q Filing for the Quarter Ended June 30, 2002, Notes to Consolidated Financial Statements, at 9.

interconnection arbitration, which was completed in August 2000 after extensive consideration by the RCA.

### **C. GCI's "Costs" as a CETC**

ACS-F is simply wrong in asserting that a CETC's loop cost is limited to only the price of the UNE loop.<sup>7</sup> As discussed in the attached Affidavit of Frederick W. Hitz, III,<sup>8</sup> GCI incurs many costs that are not included in ACS-F's UNE loop rate. GCI must pay ACS-F for collocation space. GCI must install multiplexing equipment and fiber to carry calls from the ACS-F unbundled loop to GCI's switch. And GCI has its own common costs, in addition to a portion of ACS-F's forward-looking common costs that are built into its UNE rates. These are but a few examples. Most significantly, GCI must incur the cost of addressing ACS-F's constant unlawful and discriminatory tactics to slow-roll its acceptance and provisioning of GCI orders.

The bottom line for GCI is that the total cost of purchasing unbundled loops from ACS-F far exceeds ACS-F's UNE-loop price, which measures ACS-F's "actual" costs, but does not include all of GCI's costs. GCI actions confirm these facts every day: GCI is investing heavily to develop cable telephony service to bypass ACS-F's UNE loops wherever possible.

## **II. THE SUPPORT PAYMENT PROVISIONS OF 47 C.F.R. § 54.307 ARE UNAMBIGUOUS, AND CANNOT BE MODIFIED ABSENT A RULEMAKING**

The Commission's rules explicitly authorize the payment of high cost support to CETCs based on the amount of support to which the ILEC is entitled. There is no uncertainty warranting a declaratory ruling, for ACS-F acknowledges that "[u]nder the Commission's rules, each CETC that wins a customer from ACS-F is entitled to receive the exact same level of

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<sup>7</sup> See ACS-F Petition at i, 3, 9.

<sup>8</sup> See Hitz Affidavit at ¶¶ 4-8.

support as ACS-F for each line the CETC serves ... up to the UNE price.”<sup>9</sup> Indeed, in at least six separate instances, ACS-F admits that current payments to CETCs such as GCI, based on ILEC costs, are authorized – *indeed required* – by the Commission’s rules.<sup>10</sup> Thus, ACS-F’s requested declaratory ruling would serve no purpose, for the rules provide that the Commission may “issue a declaratory ruling *terminating a controversy or removing uncertainty*.”<sup>11</sup> In this instance, there is simply no controversy to terminate or uncertainty to remove.

In truth, what ACS-F is asking the Commission to do is to change its rules without a rulemaking.<sup>12</sup> Recognizing that the Commission cannot do so, ACS-F then argues that the rules, *as presently written*, violate the Act.<sup>13</sup> Again, there is no ambiguity – the Commission has expressly spoken. In its *Universal Service First Report & Order*, the Commission expressly rejected arguments that rule 54.307 would violate section 254(e), stating that “[w]e thus disagree with commenters that assert that providing support to eligible CLECs based on the incumbents’ embedded costs would violate Section 254(e).”<sup>14</sup>

In any event, GCI fully meets Section 254(e)’s requirement that a “carrier that receives such support shall use that support only for the provision, maintenance, and upgrading of facilities and services for which the support is intended.” Section 254(e)’s reference to “facilities and services for which the support is intended” has a specific meaning. Pursuant to

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<sup>9</sup> ACS-F Petition at 9.

<sup>10</sup> See ACS-F Petition at i, 3, 7, 9, 16, 23.

<sup>11</sup> 47 C.F.R. § 1.2 (emphasis added).

<sup>12</sup> See 5 U.S.C. § 553 (requiring the FCC to provide public notice of proposed changes to its rules and an opportunity for interested persons to participate in the rulemaking).

<sup>13</sup> ACS-F Petition at 8 (“Enforcing Section 54.307 ... can and does result in a violation of Section 54.7 ... and Section 254(e) of the Act.”).

Section 254(a) and (c), the Commission, based upon recommendations from a statutorily-mandated federal-state joint board, set forth a “definition of the services that are supported by Federal universal service support mechanisms”<sup>15</sup> that is codified in rule 54.101. This definition encompasses single-party, voice grade access to the public switched network with dual tone multifrequency signalling (also known as “Touchtone” dialing), local usage, access to emergency services, access to operator services, access to interexchange services, access to directory assistance, and toll limitation for low income consumers.<sup>16</sup> The Commission’s rules further specifically provide that, in order to receive federal universal service support, a carrier must offer each of the services set forth in the regulation.<sup>17</sup>

GCI offers the required services in Fairbanks, and its costs of doing so far exceed the universal service support it receives. Indeed, because GCI’s universal service support for unbundled loops by rule is limited to the amount paid for the unbundled loop under rule 54.307, it is simply mathematically impossible for GCI not to be using federal universal service support it receives in Fairbanks solely for the provision, maintenance or upgrade of its universal service in Fairbanks.

In addition, the RCA has followed the Commission’s 254(e) safeguards. The Commission requires that, as a condition of the receipt of high-cost loop support, the state commission certify that each ETC would use the support consistent with the requirement of

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<sup>14</sup> See *In re Federal-State Joint Board on Universal Service*, Report & Order, 12 FCC Rcd 8776, 8945 (¶ 313) (1997) (“*Universal Service First Report & Order*”), *aff’d in relevant part*, *Texas Office of Public Utility Counsel v. FCC*, 183 F.3d 393 (5<sup>th</sup> Cir. 1999).

<sup>15</sup> 47 U.S.C. § 254(a)(2).

<sup>16</sup> 47 C.F.R. 54.101(a)(1)-(9).

<sup>17</sup> *Id.* § 54.101(b).

section 254(e).<sup>18</sup> In fulfilling that requirement, the RCA issued an order to all regulated ETCs, including GCI, requiring each to submit information demonstrating that all support would be used only for provision, maintenance, and upgrading of facilities and services for which the support is intended.<sup>19</sup> GCI submitted the required filing and, based on that filing, the RCA found that GCI would use the support appropriately and the RCA certified GCI's use to the FCC.<sup>20</sup>

Based on the foregoing, it is clear that the Commission's current rules require the payment of universal service support to GCI, as a CLEC designated as an ETC, on a per-line basis in the same amount paid to the ILEC, based on the ILEC's costs. On this ground alone, ACS-F's petition must be rejected. It is equally clear that payment of such support as required under rule 54.307 does not violate section 254(e), and that the Commission previously rejected such arguments during its rulemaking proceedings. ACS-F has no legal basis for its petition.

### **III. THE PAYMENT AND PORTABILITY OF USE TO CLECS, BASED ON THE AMOUNT PAID TO THE ILEC, IS APPROPRIATE POLICY AND FULLY CONSISTENT WITH THE UNDERLYING PURPOSES OF THE ACT**

Even if ACS-F had filed a petition for rulemaking, its requested change in the Commission's rules should be rejected because section 54.307 was adopted after extensive consideration by both the Joint Board and the Commission, and was intentionally structured to

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<sup>18</sup> See 47 C.F.R. § 54.314(a). In several instances, ACS-F's petition incorrectly refers to a CETC's "certification," or even "self-certifi[cation]." ACS-F Petition at 22, 34. There is no self-certification for high-cost loop support; certification is by the state regulatory commission pursuant to 47 C.F.R. § 54.314.

<sup>19</sup> See *In re Commission Compliance with Federal Requirements to Certify Proper Use of Federal Universal Service Funds by Telecommunications Carriers*, Order No. 1, Regulatory Commission of Alaska Docket No. U-01-90 (July 13, 2001).

<sup>20</sup> See *In re Commission Compliance with Federal Requirements to Certify Proper Use of Federal Universal Service Funds by Telecommunications Carriers*, Order No. 2, Regulatory Commission of Alaska Docket No. U-01-90 (Nov. 13, 2001). ACS-F's claims that the RCA "abdicated" this responsibility are entirely false.

send signals based on a competitive market.<sup>21</sup> The Commission adopted the Joint Board recommendation to make support payments portable “[i]n order not to discourage competition in high cost areas.”<sup>22</sup> The Commission was “not persuaded” by arguments that portable support based on ILEC costs was “preferential” to competitors,<sup>23</sup> concluding to the contrary that

[w]hile the CLEC may have costs different from the ILEC, the CLEC must also comply with Section 254(e), which provides that “[a] carrier that receives such support shall use that support only for the provision, maintenance, and upgrading of facilities and services for which the support is intended.” Furthermore, because a competing eligible telecommunications carrier must provide service and advertise its service throughout the entire service area, consistent with section 214(e), the CLEC cannot profit by limiting service to low cost areas. If the CLEC can serve the customer’s line at a much lower cost than the incumbent, this may indicate a less than efficient ILEC. The presence of a more efficient competitor will require that ILEC to increase its efficiency or lose customers. State members of the Joint Board concur with our determinations regarding the portability of support.<sup>24</sup>

The Commission, therefore, carefully and deliberately chose to encourage competitive entry and let the market expose inefficiencies by basing CETC support payments on ILEC costs. And the wisdom of the Commission’s policy choice is proven by the fact that GCI’s competitive entry is exposing precisely the sort of inefficiencies in ACS-F’s operations that the Commission and the Joint Board anticipated.

ACS-F recycles ILEC contentions from five years ago in arguing that payment of support to GCI based on the amount paid to ACS-F violates the goal of competitive neutrality and harms

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<sup>21</sup> ACS-F acknowledges this as well, reporting that the Commission “decided to adopt the Joint Board’s recommendation to calculate support to all ETCs based on the ILEC’s costs.” ACS-F Petition at 16.

<sup>22</sup> See *Universal Service First Report & Order*, 12 FCC Rcd at 8932 (¶ 287).

<sup>23</sup> *Id.* at 8933 (¶ 289).

<sup>24</sup> *Id.* (citations omitted).



customers by encouraging inefficient entry. This occurs, according to ACS-F, because the payment and portability of support to GCI based on the costs of ACS-F provide GCI with a “cost of goods sold” lower than ACS-F.<sup>25</sup> This argument is fundamentally flawed. As explained below, payment and portability of support to CLECs, based on the costs of the ILEC, *is* competitively neutral and retains the appropriate market signals for competitive entry. The payment of such support does not in any way affect the relative costs of goods sold by the incumbent and the competitor.

In any competitive market, competitors are likely to have different costs. In the absence of a subsidy, the market would be expected to wring out inefficiencies by allowing the competitor with lower costs to underprice the other, and by requiring the higher cost competitor to cut its costs so as to match its more efficient competitor’s offerings. Although in equilibrium the prices and costs would be expected to be the same, equilibrium is rarely, if ever, reached. Thus, cost differentials, and the battle between competitors to be the more efficient provider, are an intrinsic part of competition.

When introducing a subsidy to reduce the market price below the levels at which the carriers would otherwise offer service, the subsidy should not eliminate the healthy competitive battle to reduce costs and be the most efficient provider. An essential element of any competitively neutral system for paying universal service support is therefore that support payments in the same market for the same service not differ based on the identity of the carrier providing the service. Put another way, the universal service program “must treat all market participants equally – for example, subsidies must be portable – so that the market, and not local or federal government regulators, determines who shall compete for and deliver services to

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<sup>25</sup> See ACS-F Petition at 10.

customers.”<sup>26</sup> If the amount of universal service support paid to a CLEC were reduced because the CLEC has a lower cost structure than the ILEC, then the reduced support would skew the appropriate, market-based price signals. The Commission would be subsidizing the consumer’s choice of the ILEC over the CLEC for the provision of service, even when the CLEC is the more efficient provider.

As an example, paying both GCI and ACS-F a subsidy based on ACS-F’s costs does not at all alter the competitive balance that would exist in the absence of the subsidy. In the absence of the \$9.40 per line that ACS-F (and hence GCI pursuant to rule 54.307) receives per month in universal service support, retail rates would have to be \$9.40 per line higher in order for ACS-F to receive the same revenue per line. GCI, as the competitor, would have the opportunity to compete for and win that entire \$9.40 for every customer. And GCI would have the incentive to enter whenever it could do so profitably based on the unsubsidized amount of revenue it would receive in competition with ACS-F’s unsubsidized prices. Providing a \$9.40 subsidy to both providers simply reduces the customer’s price by \$9.40, but keeps the revenue opportunity for each carrier from serving that customer the same.

By contrast, competitive incentives and market discipline are greatly skewed from the unsubsidized scenario if a subsidy is provided to only one carrier but not the other, or to one carrier in an amount greater than the other. If ACS-F were to receive a subsidy of \$9.40, and GCI received none for serving the same subscriber with the same service, GCI would have no incentive to enter and compete unless it could be at least \$9.40 *more efficient* than ACS-F. Put another way, ACS-F could be up to \$9.40 per loop per month less efficient and more costly than

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<sup>26</sup> *Alenco Communications, Inc. v. FCC*, 201 F.3d 608, 616 (5<sup>th</sup> Cir. 2000) (noting that principles such as portability are “made necessary not only by the economic realities of competitive markets but also by [47 U.S.C. § 214(e)(1)]”).

GCI before it would make sense for GCI to enter and for a customer rationally to select GCI. Under such a system, which is essentially what ACS-F advocates, the competitive market's incentives for efficient service are dramatically blunted, and the ratepayer, through universal service fees, ends up funding *inefficient* service.

Although these economics are clearest when GCI (or any other CLEC) provides service entirely over its own facilities, these economics do not change when GCI leases a portion of its loop facilities from ACS-F as an unbundled network element. Of course, in order to send the appropriate price signals to both the ILEC and the CLEC, the unbundled network element – in GCI's case, usually an unbundled loop – must be priced correctly. However, the Commission has already issued rules defining the appropriate methodology for correctly setting the unbundled loop price: based on forward-looking economic cost. As the Commission found in its *Local Competition Order*, setting the UNE price at the forward-looking cost provides the competitor with the appropriate price signal in deciding whether to enter a new market and whether to construct its own facilities:

In dynamic competitive markets, firms take action based not on embedded costs, but on the relationship between market-determined prices and forward-looking economic costs. If market prices exceed forward-looking economic costs, new competitors will enter the market.... New entrants should make their decisions whether to purchase unbundled elements or to build their own facilities based on the relative economic costs of these options.<sup>27</sup>

ACS-F's UNE rates were arbitrated in Fairbanks according to such a forward-looking cost methodology.

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<sup>27</sup> *In re Implementation of the Local Competition Provisions in the Telecommunications Act of 1996; Interconnection between Local Exchange Carriers and Commercial Mobile Radio Service Providers*, First Report & Order, 11 FCC Rcd 15499, 15813 (¶ 620) (1996) (“*Local Competition Order*”).

When ACS-F's calculations are performed using the RCA's adjudicated cost-based UNE loop rate for Fairbanks as the measure of ACS-F's "costs," rather than ACS-F's embedded "book" costs, all purported competitive advantages to GCI disappear. Both carriers have the same monthly loop revenue opportunity, not including subsidies. ACS-F has a forward-looking loop cost of \$19.19, which is the rate GCI pays ACS for leasing the UNE loop.<sup>28</sup> Paying the \$9.40 in subsidy to both entrants, as rule 54.307 requires, maintains the competitive balance.

What ACS-F is really arguing – which it reveals by constantly asserting that its embedded costs are its "actual" costs – is that its embedded costs are actually the proper measure of its costs, and that the Commission (and the RCA acting pursuant to FCC rules) should have allowed ACS-F to price its unbundled loops based on embedded costs. Of course, it was exactly this argument that the Commission rejected in its *Local Competition Order*,<sup>29</sup> a decision that has since been upheld by the Supreme Court.<sup>30</sup> In the *Local Competition Order*, the Commission expressly found that "[t]he substantial weight of economic commentary in the record suggests that an 'embedded cost'-based pricing methodology would be pro-competitor – in this case the incumbent LEC – rather than pro-competition."<sup>31</sup> For that reason, the Commission "decline[d] to adopt embedded costs as the appropriate basis of setting prices for interconnection and access to unbundled elements."<sup>32</sup> In short, the Commission rejected embedded costs as a measure of the ILEC's true economic costs for the purposes of setting UNE prices "based on cost."<sup>33</sup>

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<sup>28</sup> This comparison does not include GCI's other loop costs, *see* Hitz Affidavit at ¶¶ 4-8, which should be included in a true comparison.

<sup>29</sup> *See id.*

<sup>30</sup> *Verizon Communications, Inc. v. FCC*, 122 S. Ct. 1646 (2002).

<sup>31</sup> *Local Competition Order*, 11 FCC Rcd at 15857-58 (¶ 705) (citation omitted).

<sup>32</sup> *Id.* at 15858 (¶ 705).

<sup>33</sup> 47 U.S.C. § 251.

Unless the Commission accepts ACS-F's premise that forward-looking UNE loop prices are below-cost subsidies, ACS-F's arguments cannot make sense economically, and will always blunt market forces seeking to push service to the most efficient provider. This fact is clearly demonstrated by Figure 1 in ACS-F's petition.<sup>34</sup> ACS-F's table shows a "Post Loop-Support Cost" to ACS-F of \$24.11, and a comparable cost to GCI of \$9.79. These figures are based on the use of ACS-F's embedded "book" loop cost of \$33.51 to establish ACS-F's costs, and the use of ACS-F's forward-looking, cost-based UNE loop rate to set GCI's costs. But GCI's purported "advantage" of \$14.32 is precisely the same, with or without the subsidy – that is, it is exactly the same difference as would exist in the absence of support to either carrier. Moreover, the difference disappears entirely as ACS-F's embedded loop costs are reduced to its forward-looking costs.

Moreover, ACS-F's own history demonstrates the extent to which embedded "book" cost is a regulatory fiction that in no way constitutes ACS-F's "actual" costs. The embedded base simply represents amounts that were booked to regulatorily defined accounting categories by ACS-F or, more likely, one of its predecessors. This system itself has been twice transferred, with the most recent acquisition occurring after the enactment of the 1996 Act and the FCC's implementing rules (including rule 54.307), following the opening of the Anchorage market, and after GCI had requested interconnection and lifting of the rural exemption for Fairbanks. These transactions severed any link between the regulatory books and ACS-F's own historical investment costs. These are simply not "actual" costs.

The CLEC's decision as to whether to build its own facilities or to use UNE loops from the ILEC also remains unaffected by the current USF system. The relevant comparison to the

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<sup>34</sup> See ACS-F Petition at 11.

CLEC is the cost of adding its own loops compared to the UNE loop rate. In either event, the CLEC receives the same amount of USF support. Again using the Fairbanks market as an example, if GCI can add its own loops for less than the UNE rate of \$19.19, GCI has an incentive to do so; USF support does not distort the incentive, because the same amount is received whether GCI buys UNEs or builds facilities. Distortion of this correct price signal would only result if, as proposed by ACS-F, payment of USF support varied depending on whether GCI built its own facilities or purchased UNEs.

Current price signals are working. GCI will begin to deploy loops using its cable television facilities in Anchorage this year and will later do so in Fairbanks. Under the current UNE loop rate and the payment of portable USF support, GCI still retains the incentive to deploy its own loop facilities rather than continuing to rely on the UNE loops from ACS-F, and indeed it is doing so. Thus, ACS-F's claims that GCI has no incentive to, and will not, build its own loop facilities is simply wrong on the facts.<sup>35</sup>

Rather than seeking a regulatory solution to its problems, ACS-F should seek to control its own costs. The reason that ACS-F has a higher cost of goods sold than GCI is that ACS-F's embedded loop cost is unreasonably high. This Commission should be concerned, for example, about the fact that ACS-F's embedded loop cost is \$33.51 when its current, forward-looking cost

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<sup>35</sup> GCI does not generally choose to install copper loop plant because GCI does not have an existing backbone system to which it can add to reach areas of new construction, and GCI's technology of choice is a hybrid fiber/coaxial system, not a copper loop system. ACS-F's allegation that GCI advises customer to initially obtain new service from ACS, then convert to GCI, is actually an attempt by ACS to cover up its illegal, ongoing, and pervasive discrimination against GCI. In numerous instances, GCI has been informed by ACS-F that no loop facilities exist to serve a particular customer, only to have sufficient facilities immediately appear as soon as the customer requests service from ACS. ACS-F's suggestion that a customer would go through the hassle of obtaining service from ACS-F – including the completing of initial applications, payment of security deposits, and arranging appointments for installation – only to

is only \$19.19. Even more significantly, this Commission should investigate why ACS-F's embedded loop cost has increased by 14 percent, from \$29.43 to \$33.51, in just three years.<sup>36</sup>

#### **IV. ACS-F'S PROPOSAL TO BASE USE SUPPORT TO CLECS ON THE CLECS' COSTS IS UNWORKABLE.**

ACS-F assures the Commission that its plan can be "immediately implemented" and "will not impose a significant burden" on CETCs, or, presumably, on the Commission itself.<sup>37</sup> In fact, even a cursory analysis of ACS-F's plan reveals how difficult and counter-productive its implementation would be.

As an initial matter, ACS-F is simply incorrect in its assertion that GCI has no material loop cost in addition to the UNE loop rate of \$19.19 paid to ACS-F.<sup>38</sup> In fact, GCI has substantial additional costs that the Commission would have to consider in determining GCI's "costs" for support purposes, which add no less than \$9.37 to GCI's loop costs, and the true amount is likely to be even higher.<sup>39</sup> In the Fairbanks market, GCI has invested more than \$2 million to collocate equipment at ACS-F's host switch and at one remote. Additionally, GCI has a transport system to link those locations to GCI's switch in Fairbanks. The equipment that GCI has collocated at the ACS-F switch and remote switch is generally comparable to digital loop carriers and line concentrators that are used by incumbent LECs and included in the embedded loop cost of the incumbent LEC. Similarly, in conjunction with such equipment, the investment

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then repeat the process again with another carrier, GCI, simply demonstrates how strongly customers prefer GCI's service to that of ACS.

<sup>36</sup> Because ACS-F is a member of the NECA Common Line Pool, its loop costs are not subject to direct scrutiny in the FCC tariff process.

<sup>37</sup> See ACS-F Petition at 35.

<sup>38</sup> See ACS-F Petition at i, 3, 9.

<sup>39</sup> See Hitz Affidavit at ¶ 9.

or lease of transport facilities to transport the loop signals to the switch also constitute embedded loop costs.<sup>40</sup>

GCI also has substantial additional costs that would appropriately be classified as loop costs. GCI, like ACS-F, has substantial overhead costs associated with loops. ACS-F argues that, pursuant to Part 36, overhead costs are assigned in proportion to *investment* in loops and, since GCI does not have significant investment in loops, GCI would not be able to allocate overhead to loops.<sup>41</sup> However, Part 36 does not apply to CLECs like GCI, and ACS-F's proposed overhead allocation is artificial and not competitively neutral. Although investment may have been a reasonable method to allocate overhead for ILECs that traditionally incurred all investment costs of the system, investment would not be a reasonable method to allocate overhead for a CLEC that has no such investment. The fact that there is no such investment does not mean that the overhead costs do not exist, and it does not mean they are not related to loop costs; it just means that, for a CLEC, investment is not a reasonable basis to allocate the associated costs. An alternative method of allocating overhead, based on factors other than investment, would have to be developed for CLECs.<sup>42</sup>

GCI also serves substantial numbers of customers entirely with its own facilities, without using UNEs from ACS-F, and will increasingly do so as it implements cable telephony. GCI's costs per line served of its cable infrastructure will predictably be extremely high in the early stages of cable telephony deployment, but will fall as the number of loops served on that plant increases. A system of support based on CLEC costs will therefore be subject to wide variations in support over time. Moreover, there is certainly no basis for creating a universal service

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<sup>40</sup> See Hitz Affidavit at ¶ 6.

<sup>41</sup> See Affidavit of Thomas R. Meade, appended to the ACS-F Petition as Exhibit B, at 3-4.



support system that gives CLECs the lower of their own costs or the ILEC's embedded costs. Such a system would amount to blatant incumbent protection.

In order to establish GCI's actual loop cost – even for loops obtained as UNEs – the Commission would have to undertake full-scale analysis of GCI's cost of providing service, and similar analysis of other CLECs. The Commission would, in essence, be doubling its regulatory review of costs in competitive markets, rather than reducing it. This result is totally contrary to the Act's purpose to develop a “pro-competitive, de-regulatory national policy....”<sup>43</sup>

Furthermore, basing USF support to a CLEC on the CLEC's cost would import all of the negative incentives of “cost plus” regulation. CLECs would then have the same incentive as ILECs to “gold plate” systems and exaggerate costs in order to maximize subsidies. That is precisely the type of regulatory system that should be phased out, not duplicated.

An acceptable alternative to the payment of USF support to CLECs based on the embedded cost of the ILECs would be to base payment of USF to both the CLEC and the ILEC on a forward-looking cost methodology. The Commission has already adopted such a system for high cost support for non-rural carriers. Like the existing system, such an approach would treat all carriers equally and would retain correct price signals, as required by both the Act and policy considerations.<sup>44</sup> Predictably, however, rate of return carriers such as ACS-F strongly opposed the setting of their USF support based on a forward-looking cost methodology.<sup>45</sup> Instead, those

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<sup>42</sup> See Hitz Affidavit at ¶ 7.

<sup>43</sup> H.R. Rep. No. 104-458, at 1 (1996).

<sup>44</sup> See, e.g., *Alenco Communications*, 201 F.3d at 616; *Local Competition Order*, 11 FCC Rcd at 15813 (¶ 620).

<sup>45</sup> ACS-F's predecessor ILEC in Fairbanks filed comments in August 1996 praising the use of ILEC “actual recorded costs” as a basis for USF payments, not just for incumbents *but also for competitive carriers*. PTI praised the use of ILEC embedded costs for CLECs as “specific[ ] and sufficien[t],” “verifiable,” not amenable to “over-recovery,” “technologically neutral,” and “the

carriers strongly preferred that USF continue to be based on embedded costs and, largely as an accommodation to those carriers, the Commission allowed continued use of embedded costs for rate-of-return carriers. ACS-F should not be heard now to complain about this accommodation.

Finally, ACS-F's complaints regarding the effects of disaggregation of USF and UNE prices, or the lack thereof,<sup>46</sup> should be ignored. Pursuant to the provisions of the Commission's decision in the *Rural Task Force Order*,<sup>47</sup> ACS-F had wide discretion to choose its preferred approach to disaggregation of its USF support. ACS-F could have, for example, prepared a highly granular disaggregation plan, but such a plan would have required ACS-F to seek RCA approval. Instead, ACS-F chose to self-certify its own disaggregation filing,<sup>48</sup> and because such plans are not subject to state commission review, this Commission appropriately limited the number of cost zones that such a self-certified plan can establish.<sup>49</sup> Furthermore, ACS-F had an opportunity to seek disaggregated UNE loop rates in the arbitration proceedings.<sup>50</sup> However,

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best economic signal for competitive entry," giving "second entrants real-world and real-time information on the current costs of service in any particular rural serving area." Comments of Pacific Telecom, Inc., *In re Federal-State Joint Board on Universal Service*, CC Docket No. 96-45 (filed Aug. 2, 1996).

<sup>46</sup> See ACS-F Petition at 30-33.

<sup>47</sup> See *In re Federal-State Joint Board on Universal Service, Multi-Association Group (MAG) Plan for Regulation of Interstate Services for Non-Price Cap Local Exchange Carriers & Interexchange Carriers*, Fourteenth Report & Order, Twenty-Second Order on Reconsideration, & Further Notice of Proposed Rulemaking in CC Docket No. 96-45, & Report & Order in CC Docket No. 00-256, 16 FCC Rcd 11244, 11302 (¶ 144) (2001) ("*Rural Task Force Order*").

<sup>48</sup> ACS of Fairbanks, Inc., *Disaggregation and Targeting Plan* (filed May 15, 2001). The Regulatory Commission of Alaska's website confirms ACS-F's selection of "Path 3" disaggregation. See < [http://www.state.ak.us/rca/hot\\_topics/Path\\_Docket\\_list.xls](http://www.state.ak.us/rca/hot_topics/Path_Docket_list.xls)>.

<sup>49</sup> *Rural Task Force Order*, 16 FCC Rcd at 11304 (¶ 151) (noting that the two-cost-zone limitation was necessary to ensure that self-certified disaggregation occurred "in a competitively neutral manner").

<sup>50</sup> "We believe ... that ACS had the opportunity to advance unbundled network element prices based on geographic zones during the arbitration process and would have strongly advocated such an approach if deaveraging were necessary to its ability to compete in the market. ACS did

ACS-F did not even propose the adoption of disaggregated UNE loop rates in that proceeding.<sup>51</sup>

ACS-F should not be heard to complain about disaggregation, or lack thereof, when the extent of disaggregation is largely the result of its own actions.

## **V. CONCLUSION**

ACS-F's claim that GCI's receipt of USF support is contrary to the Act and the Commission's rules is plainly wrong. The Commission's rules explicitly provide that USF support shall be paid to CETCs in the same amount, per line, as paid to the ILEC.

ACS-F's far ranging policy arguments are also misplaced. In order to maintain appropriate price signals and competitive neutrality, the same amount of support, per line, must be paid to all carriers providing comparable local exchange service. The Commission's current rule is consistent with that principle.

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not do so." *In re Request by GCI Communication Corp. d/b/a General Communication, Inc., & d/b/a GCI for Designation as a Carrier Eligible To Receive Federal Universal Service Support Under the Telecommunications Act of 1996 for the Fairbanks, Fort Wainwright, & Juneau Areas*, Order No. 1, Regulatory Commission of Alaska Docket No. U-01-11 (Aug. 28, 2001).

<sup>51</sup> The arbitration was conducted under "last best offer", or "baseball", arbitration. ACS-F's final best offer included a single, averaged UNE loop rate for the entire Fairbanks service areas. See Hitz Affidavit at ¶ 3.

For all of the foregoing reasons, GCI urges the Commission to reject the petition filed by ACS-F.

Respectfully submitted,

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